P 53/989-2

FET

Foreign Economic Trends and Their Implications for the United States

AUGUST 1989

PHILIPPINES

FET 89-90
Frequency: Semiannual
Supersedes: 89-15

PREPARED BY
AMERICAN EMBASSY MANILA

U.S. DEPARTMENT OF COMMERCE
International Trade Administration
Washington, D.C. 20230

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PHILIPPINES: KEY ECONOMIC INDICATORS
(In millions of U.S. dollars unless noted)

	1986	1987	1988 p/	1989 (Proj.) a/
Domestic Economy				
Population (est. in millions)	56.0	57.4	58.7	60.1
Population growth (% est.)	2.4	2.4	2.4	2.4
GDP in current dollars r/	30,763	34,442	39,192	43,761
GNP in current dollars r/	30,153	34,198	39,050	43,120
Per capita GDP, current dollars r/	$549	$600	$667	$728
GDP in pesos (1972=100) % change r/	1.54	4.70	6.36	6.5
GNP in pesos (1972=100) % change r/	1.98	5.91	6.74	6.5
Consumer price index, average % change	0.8	3.8	8.8	8.0
Production and Employment				
Labor force (1,000s)	21,362	22,563	23,449	24,414
Unemployment rate (%)	11.8	11.2	9.6	8.8
Industrial prod. (1972=100) % change r/	(2.1)	7.8	8.6	8.2
Gov't budget deficit as % of GNP	(5.1)	(2.4) r/	(2.5)	(1.6)
Balance of Payments				
Exports (FOB)	4,842	5,720	7,074	8,040
Imports (FOB)	5,044	6,737	8,159	9,560
Trade balance	(202)	(1,017)	(1,085)	(1,520)
Current-account balance	996	(444) r/	(373)	(959)
Foreign direct investment (inflow)	186	439	1,077	987
Foreign debt, total forex liab yr-end	28,256	28,649	27,915	30,568
Debt-service paid (princ. & int.)	2,936	3,057	3,221	3,220
Debt-service as % of goods & serv exports	34.0	33.3	30.2	26.6
Foreign exchange reserves	2,459	1,959	2,059	3,485
Average exchange rate (in Pesos/US$)	20.386	20.567	21.095	21.70
Foreign Investment (CB registrations) b/				
Total (cumulative)	2,732	2,830	2,902	NA
U.S. (cumulative)	1,552	1,620	1,649	NA
U.S.-Phil. Trade (Philippine figures)				
U.S. exports to Phil. (FOB)	1,256	1,488	1,715	2,008
U.S. imports from Phil. (FOB)	1,717	2,064	2,516	2,935
U.S. trade balance with Philippines	(461)	(576)	(801)	(927)
U.S. share of Phil. exports (%)	35.5	36.1	35.6	36.5
U.S. share of Phil. imports (%)	24.9	22.1	21.0	21.0
U.S. Bilateral Aid (fiscal year)	377.9	439.6	254.3	511.0
Economic (includes food aid)	275.3	339.6	126.7	384.4
Military (includes training)	102.6	100.0	127.6	127.6

Principal U.S. exports (CY1988): electric machinery, $206 M; nonelectric machinery, $197 M; chemicals & products, $196 M; cereals & cereal preparations, $178 M; intermediate goods on consignment, $616 M c/.

Principal U.S. imports (CY1988): electric machinery, $226 M; wearing apparel, $220 M; coconut oil, $184 M; fruits & vegetables, $113 M; consignment imports, $1.083 M c/.

a/predominantly government targets, b/principally exercised to assure repatriation rights, c/mostly for semiconductors and garments, p/preliminary, r/ revised, NA/not available SOURCES: Government of the Philippines, USAID

SUMMARY

Philippine economic output, as measured by gross national product (GNP), posted its third consecutive year of real growth in 1988. Up 6.7 percent, total output finally recovered to its pre-crisis peak. The economic expansion was still basically consumer led. Investment, particularly in durable equipment, continued a strong, sustained recovery. For the year, domestic investment climbed 19 percent to reach 16 percent of GNP.

Most recent government targets put GNP growth at 6.5 percent each year until 1992. Private forecasters, expecting somewhat slower export performance and budgetary constraints on public spending, see 5.5 to 6 percent growth for 1989. Steady growth in domestic investment is forecast for the near term, reaching a healthy 24 percent of GNP by 1992.

Monthly year-to-year inflation rates averaged 8.8 percent in 1988 and remained at one-digit levels throughout the year despite the upward pressure exerted by a consumer-led recovery. Except for savings deposits, real interest rates remained positive, though at more moderate levels than in 1987.

The country's overall balance-of-payments (BOP) surplus more than doubled from $264 million in 1987 to $516 million in 1988. That gain reflected improvements in both current and capital accounts, as well as the positive impact of net currency revaluation adjustments. Without new loans and rescheduling, the BOP would have yielded a deficit of $1.6 billion.

December 1988 closed with the peso-dollar exchange rate at 21.335, a modest 2.6 percent annual depreciation. The Central Bank's gross international reserve (GIR) position at the end of 1988 was $2 billion, sufficient for 2.1 months' worth of import requirements. As of March 1989, the Central Bank's GIR stood at $1.8 billion, adequate for only 1.8 months of imports.

In 1988, a total merchandise trade of $15,233 million (22 percent over 1987) surpassed the 1981 peak of $13,668 million. With exports rising 24 percent and imports gaining 3 percent, between 1981 and 1988, last year's trade deficit of $1,085 million was 46 percent narrower than 1981's deficit of $2,224 million. The United States' $801 million trade deficit with the Philippines for 1988 was 39 percent larger than the previous year's deficit of $576 million.

Domestic Economic Performance

Philippine economic output, as measured by gross national product (GNP), posted its third consecutive year of real growth in 1988. Up 6.7 percent, total output finally recovered to its pre-crisis peak. Per capita GNP continued to improve but is not expected to regain its pre-crisis level for another three years.

On the supply side, the industrial sector contributed the largest share (41 percent) to overall GNP expansion. That sector's output grew 8.6 percent, surpassing that of agriculture (3.5 percent) and services (6.6 percent). Manufacturing contributed the bulk (80 percent) of the growth in industrial sector production, which reflected a broad-based demand recovery ranging from consumer items to capital equipment.

The agricultural sector's growth would have been higher if not for the adverse effect of inclement weather on commercial crop harvests. Gains in livestock, poultry and fishery pulled up the marginal (1 percent) gain in crop production.

GNP BY PRODUCTIVE SECTOR
JANUARY-DECEMBER 1987 & 1988
(At Constant 1972 Prices)

SECTOR	In Million Pesos 1987	1988	Year-to-Year Growth 1986-87	1987-88
AGRI, FISHERY, FORESTRY	26,834	27,771	-1.02	3.49
INDUSTRY	30,590	33,205	7.73	8.55
Mining & Quarrying	1,547	1,615	-1.72	4.40
Manufacturing	23,168	25,251	6.68	8.99
Construction	3,967	4,344	17.30	9.50
Basic Utilities	1,908	1,995	10.74	4.56
SERVICE SECTOR	38,039	40,558	6.63	6.62
Transport & Comm.	5,251	5,487	2.86	4.49
Trade	15,153	15,832	5.69	4.48
Finance & Housing	5,832	6,200	20.72	6.31
Private Services	6,106	6,437	1.11	5.42
Government Services	5,697	6,602	6.25	15.89
GROSS DOMESTIC PRODUCT	95,463	101,534	4.70	6.36
Net Factor Income	(666)	(348)		
GROSS NATIONAL PRODUCT	94,797	101,186	5.91	6.74

Source: Philippine National Income Accounts, April 1989

On the demand side, personal consumption, which contributed over 66 percent of overall economic expansion, continued to provide the major impetus to economic growth. Per capita consumer spending, which declined from 1984 to 1986, recovered the peak level posted in 1981 following higher average incomes and reduced unemployment.

Investment in construction, durable equipment and inventory (gross capital formation) expanded by 19 percent. That rate was not quite sufficient for investments to lead the recovery. However, it is encouraging to note that durable equipment (in contrast to inventory stockpiling in 1987) accounted for the bulk of that expansion. Investment in durable equipment accelerated from 16 percent in 1987 to 29 percent in 1988 as industries embarked on new programs to address production capacity constraints. Nevertheless, the 1988 level remained 40 percent below the 1981 peak. Its current share of GNP (7 percent) is at only half what it was eight years ago. With economic output back on track, continued robust growth in productive capacity will be crucial to sustaining general economic expansion.

Most recent government targets put GNP growth at 6.5 percent each year until 1992. Private forecasters, expecting somewhat slower export performance and budgetary constraints on public spending, see 5.5 to 6 percent growth for 1989.

Prices: Monthly year-to-year inflation rates averaged 8.8 percent in 1988 and remained at one-digit levels throughout the year despite the upward pressure exerted by a consumer-led recovery. A cautious monetary policy and expansions in productive capacity moderated inflationary tendencies. Year-to-year inflation peaked at 9.7 percent in April and ended the year at 9.1 percent.

The government has expressed its resolve to keep inflation within the single digits. Average inflation for 1989 has been targeted at 8 percent. Anticipated increases in oil prices and legislated minimum wages could push the inflation rate somewhat higher than the targeted level.

Except for savings deposits, real interest rates remained positive, though at more moderate levels than in 1987. Nominal bank lending rates, influenced by higher rates on Treasury Bills and Central Bank open market instruments, inched upward from an average of 13.3 percent in 1987 to 16 percent for 1988. Higher rates on government debt reflected efforts to rein in liquidity, support the value of the peso and fill budget gaps left by shortfalls in external financing.

Further increases in financial costs will depend on the government's ability to control the deficit and on the Central Bank's reaction to further drops in the value of the peso. Those increases will probably be moderate because of mounting concern that high interest rates will retard investment growth.

External Account: The country's overall balance-of-payments (BOP) surplus more than doubled from $264 million in 1987 to $516 million in 1988. That gain reflected improvements in both current and capital accounts, as well as the positive impact of net currency revaluation adjustments. Without new loans and rescheduling, the BOP would have yielded a deficit of $1.6 billion.

The current account deficit narrowed by $71 million. A $216 million expansion in net transfers (aid and grants) more than offset wider gaps in both merchandise and services trade. While merchandise exports grew at a somewhat faster pace than imports, imports continued to exceed exports in nominal value. Meanwhile, the services account shifted from break even in 1987 to a deficit of $77 million in 1988. Although service receipts improved by $152 million due mainly to personal remittances by Filipino overseas contract workers and to operating expenditures by multinationals, service outflows expanded by $229 million. That basically reflected higher interest payments and, consistent with import growth, greater outlays for freight and merchandise insurance.

The capital account surplus widened from $421 million to $492 million. Net direct investments, boosted by debt-to-equity swaps, more than tripled from its 1987 level. The $660 million gain more than made up for drops in both the medium- and long-term (MLT) and short-term capital accounts. The short-term capital account shifted from a positive to a negative balance following heavy repayments under existing trade facilities. The MLT account also shifted from a surplus ($159 million) to a deficit ($329 million) as higher repayments (which partly reflected the accounting treatment of debt-to-equity conversions) outstripped inflows. The slow implementation of public investment projects, which the government is trying to address through its Project Facilitation Committee, limited potentially higher drawdowns from already committed foreign assistance funds.

Government projections for 1989 show an overall BOP surplus of $1.6 billion, more than triple that in 1988. Those projections hinge on bridging a $1.4 billion financing gap, about half of which is being requested from foreign commercial banks. Fresh investments will also be required to take up the slack in debt-to-equity conversions since that program is currently very

restricted due to inflationary concerns. Nevertheless, the government has declared its intention to review the debt-to-equity process and have a new program in place by the end of the year.

Foreign Exchange: December 1988 closed with the peso-dollar exchange rate at 21.335, a modest 2.6 percent annual depreciation. Without Central Bank intervention, bank economists had expected the peso to weaken gradually by 4-5 percent in view of a widening trade gap and a narrowing cushion of international reserves. The Central Bank used a combination of dollar sales and higher domestic interest rates to curb what would have been a larger drop. Despite an even wider trade gap for 1989, most observers believe that the Central Bank will keep the annual depreciation of the peso under 3 percent for the year.

The Central Bank's gross international reserve (GIR) position at the end of 1988 was $2 billion, sufficient for 2.1 months' worth of import requirements. Foreign exchange purchases in November and December as well as external credits negotiated late in the year reversed the decline from $1.8 billion in May to $1.5 billion in October.

As of March 1989, the Central Bank's international reserve position stood at $1.8 billion, adequate for only 1.8 months' worth of imports. The Central Bank has targeted a reserve level of $3.5 billion by year-end, consistent with a more comfortable three months' worth of import requirements. Central Bank officials project a steady improvement in the GIR level by the second half of 1989, following expected inflows from multilateral institutions as well as new loans to be negotiated with the country's commercial bank creditors.

Investment: A strong and sustained recovery of investment was the centerpiece of economic performance during 1988. By mid-year, production fully recovered to pre-crisis levels. The consequent need for capacity expansion pushed third quarter investments in durable equipment to record levels. For the year, domestic investment climbed 19 percent to reach a level of 16 percent of GNP. Similarly, foreign investment leapt 130 percent, largely due to the consummation of a large number of debt-to-equity swaps.

Steady growth in domestic investment is forecast for the near term, reaching a healthy 24 percent of GNP by 1992. Reported foreign investment figures, now well over pre-crisis levels, may dip somewhat before a revised debt-equity program is put in place.

Fiscal Policy: Just before the new year, the Philippine Congress approved a national expenditure budget for CY1989 totaling 227.4 billion pesos ($10.5 billion). In March 1989, after reviewing its fiscal policy in order to prepare a letter of intent for the IMF, the Philippine Government decided on a cash obligation budget for 1989 of 165.2 billion pesos, with a cash deficit of 15.3 billion pesos. To meet these targets, the Bureau of Internal Revenue was tasked with collecting 79 billion pesos, while the Customs Bureau needed 35 billion. These targets are substantially above 1988 goals, which were not attained. Despite the new higher targets, a concerted effort to boost collections for 1989 yielded first quarter revenues which were less than 3 percent below the goal. Nevertheless, many analysts were skeptical that the low deficit target for 1989 could be attained.

Labor Developments: The industrial relations scene has improved markedly since the turbulent period of 1986. In 1987, days lost due to strikes declined by almost 50 percent compared with 1986. 1988 saw a further decline of 20 percent from the 1987 level. Strike activity was up in the first half of 1989 as large numbers of contracts are due for renegotiation.

Unemployment declined from 9.1 percent in January 1988 to 8.4 percent in January 1989. The National Statistics Office reported the growth of employment in the same period at 732,000, with total employment of 21.56 million people. Employment growth must continue in this range to keep up with population growth.

Foreign Trade: Philippine foreign trade marked a milestone in 1988. Five years after the decline, trade levels recovered to, and exceeded, pre-crisis levels. Total merchandise trade of $15,233 million, an increase of 22 percent over 1987, surpassed the 1981 peak of $13,668 million. With exports rising 24 percent and imports gaining 3 percent between 1981 and 1988, last year's trade deficit of $1,085 million was 46 percent narrower than 1981's deficit of $2,224 million.

Exports, heavily fed by imported inputs for the manufacturing sector, grew by nearly 24 percent to $7,074 million in 1988, largely on the strength of nontraditional products (NTs) which earned $5,361 million. Consigned exports, particularly electronics and garments, which contributed the largest share (50 percent) to overall NTs growth of 28 percent, expanded by 25 percent. They accounted for a fairly stable 40 percent share of total exports during the previous two years relative to a 35 percent share in 1986. The expansion in the production capacity of local semiconductor firms coupled with product

diversification helped the electronics industry to cope with increasing world demand. At the same time, sustained demand for wearing apparel and accessories from both quota and nonquota countries resulted in the 19 percent rise in shipments of these goods. Strong commodity prices and greater demand for copper metal and shrimp and prawns contributed to the strong performance of the NTs. Accounting for nearly 76 percent of total exports last year, compared with 73 percent in 1987, NTs will continue to dominate the export market.

PRINCIPAL MERCHANDISE EXPORTS OF THE PHILIPPINES, CY1988
(FOB value in million U.S. dollars)

Product	1988	1987	Increase (Dec) Value	In Pct
TOTAL, ALL EXPORTS	7,074	5,720	1,354	23.7
NONTRADITIONAL EXPORTS	5,361	4,197	1,164	27.7
Elec & Elec Eqpmt a/	1,476	1,119	357	31.9
Garments & Textiles b/	1,388	1,166	222	19.0
Fish & Processed Food	491	333	158	47.4
Copper/Nickel/Iron Ore	381	238	143	60.1
TRADITIONAL EXPORTS	1,606	1,367	239	17.5
Coconut Products	578	561	17	3.0
Mineral Ores & Conc	383	224	159	71.0
Forest Products	261	243	18	7.4
O T H E R	107	156	(49)	(31.4)

a/ Mostly electronic goods assembled from consignment imports
b/ Mostly garments made from materials imported on consignment
Source: Foreign Trade Statistics of the Philippines

In 1988, traditional exports continued to increase, though at a slower rate of 17 percent, reaching $1,606 million. Exhibiting the largest aggregate increase of 71 percent were mineral ores and concentrates. This was due to larger volume shipments, generally rising prices (especially for copper), and fairly stable gold prices in the world market. A 40 percent increase in the prices of coconut oil and copra in the world market more than offset substantial declines in the shipment of these commodities. Except for pineapples, whose export value slightly decreased after prices dipped, traditional products contributed significantly to larger 1988 exports.

PRINCIPAL MERCHANDISE IMPORTS OF THE PHILIPPINES, CY 1988
(FOB value in million U.S. dollars)

Product	1988	1987	Increase (Dec) Value	In Pct
TOTAL, ALL IMPORTS	8,159	6,737	1,422	21.1
RAW MAT & INTERMED GOODS	4,174	3,426	748	21.8
M/A for Mftr Elec Eqpmt a/	910	767	143	18.6
Chemical Compounds	367	332	35	10.5
Embroideries a/	377	334	43	12.9
Tex Yarn, Fabric & M-U Art	324	279	45	16.1
Iron & Steel	475	340	135	39.7
CAPITAL GOODS	1,735	1,210	525	43.4
NonElec Machinery	708	537	171	31.8
Elec Mac & Apparatus	579	451	128	28.4
MINERAL FUELS & LUBRICANTS	1,096	1,249	(153)	(12.2)
Petroleum Crude	919	1,062	(143)	(13.5)
CONSUMER GOODS	740	547	193	35.3
Food	548	368	180	48.9
O T H E R	414	305	109	35.7

a/ Mostly consignment imports
Source: Foreign Trade Statistics of the Philippines

Imports, however, continued to outpace exports in nominal terms. A sustained pace of economic activity, in order to meet growing demand for manufactured goods here and abroad, continued to exert pressure on imports which rose by 21 percent to $8,159 million in 1988. Robust import demand starting from a higher base, widened the merchandise trade gap to a deficit of $1,085 million, despite a faster growth rate for exports. Raw materials and intermediate goods (about a third on consignment for later export), accounted for 51 percent of total merchandise imports. Large investments in new plant machinery and replacement parts, such as those related to textiles, garments and electronics, brought in $1,735 million worth of capital goods. Mineral fuels imports posted a 12 percent decline in value, due to lower average prices for petroleum crude (from $17 per barrel in 1987 to $13.3 per barrel in 1988). All other imports showed marked increases. Growing domestic and foreign investments helped to fuel the country's demand for imports.

The United States' $801 million trade deficit with the Philippines for 1988 was 39 percent larger than the previous year's deficit of $576 million. The United States absorbed

36 percent of the country's shipment of goods, principally garments and textiles, and electrical equipment while supplying 21 percent of imports led by electric and nonelectric machinery, and chemicals. Japan and EEC were the other major trade partners but with much smaller shares of the country's total trade at 17 percent and 15 percent respectively as against the 28 percent share for the United States. Among the Philippines' major trade partners, surpluses were realized only with the United States and EEC.

The government targets a 16 percent growth in 1989 total trade to $17,600 million. The trade gap could swell to an estimated $1.5 million with imports beating exports by about 18 percent.

Prospects for the Future: Current indications are that the Philippine economic recovery should continue through the medium term. A major factor is domestic investment which must increase substantially from the current 16 percent of GDP if the expansion is to become self-sustaining. Indications are that substantial increases have begun as consumer and basic industries have run up against capacity constraints. Foreign investments may also continue to increase.

Another major factor to watch is external financing. Some analysts have long predicted that the Philippines would encounter a finance gap in 1989 as the expansion, and the import growth, continued. The modest run-down in reserves since mid-1988 would seem to bolster that view. Nevertheless, additional financing, principally from the IMF, the World Bank, bilateral and commercial creditors, should alleviate a good portion of the external finance constraint for 1989. The major question is whether available finance will be sufficient to build reserves all the way up to target, sufficient for three months' worth of imports.

The current prospect, therefore, is for continued growth at about the 6 percent level for the next several years. While somewhat below the government target of 6.5 percent, this growth should carry the Philippines to recover the previous per capita GNP peak in 1992. Growth after that time will depend increasingly on the development of export industries and markets.

IMPLICATIONS FOR THE UNITED STATES

Given domestic and foreign investor confidence in the Philippines, continuing import liberalization and the country's faithful servicing of its external debt, continued economic expansion should offer excellent opportunities for U.S. businesses.

Private sector foreign investments will continue to be an important component in sustaining the country's ongoing economic recovery. For 1989, the government has added 25 new industries to the list of 199 pioneer industries and

additional incentives are being offered offered to investors. Private sector investor interests are active in the manufacturing, mining, agribusiness and service sectors.

U.S.- Philippine Trade Opportunities: In 1988, U.S. exports to the Philippines increased by 15.2 percent, compared with the year before. Principal U.S. exports included electric and nonelectric machinery, chemicals and products, and cereals. The following sectors, ranked according to priority, offer potential for U.S. exporters:

1. Industrial Chemicals
2. Telecommunications Equipment
3. Pumps, Valves, and Compressors
4. Electronic Power Equipment
5. Metalworking/Machine Tool Equipment
6. Textile Machinery
7. Medical Equipment
8. Food Processing & Packaging Equipment
9. Mini & Micro Computers
10. Avionics and Ground Support Equipment
11. Laboratory & Scientific Equipment

U.S. Trade Promotion Events in the Philippines:

August 1-29, 1989	Made in USA (PIP), RC
November 13-17, 1989	Phil Medic '89, TFO
	Marketing USA Catalog Exhibition, RC
	Multi State Trade Days, TM
February 6-7, 1990	U.S. Air-conditioning and Refrigeration Machinery, VC
	Med/Lab, RC
March 1990	Electric Power Generator Equipment, TM
April 19-20, 1990	Telecommunications, SM
May 1990	Food Production, VCE
	Engineering & Construction Services, TM
September 1990	Avionics Ground Support Equipment, TM

TM - Trade Mission
SM - Seminar Mission
VCE - Video Catalog Exhibition
TFO - Trade Fair (Overseas Procured)
PIP - Post-Initiated Promotion
RC - Regular Catalog Exhibition

Prospective U.S. investors and exporters can take advantage of the expanding opportunities the Philippines has to offer by contacting their U.S. Department of Commerce district office or

American Embassy Manila
Foreign Commercial Service
APO San Francisco, CA 96528.